

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name Bay County Road Commission	County Bay
Audit Date 12/31/04	Opinion Date 4/7/05	Date Accountant Report Submitted to State: 5/31/05	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:


1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ Yes ☒ No 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ Yes ☒ No 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☒ Yes ☐ No 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ Yes ☒ No 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ Yes ☒ No 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ Yes ☒ No 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ Yes ☒ No 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ Yes ☒ No 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ Yes ☒ No 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	✓		
Reports on individual federal financial assistance programs (program audits).			✓
Single Audit Reports (ASLGU).			✓

Certified Public Accountant (Firm Name) Stewart, Beauvais & Whipple PC			
Street Address 1979 Holland Avenue	City Port Huron	State MI	ZIP 48060
Accountant Signature 		Date 5/31/05	

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

ANNUAL FINANCIAL STATEMENTS
WITH SUPPLEMENTARY INFORMATION

FOR THE YEAR ENDED DECEMBER 31, 2004

Stewart,
Beauvais
& Whipple P.C.

CERTIFIED PUBLIC ACCOUNTANTS



BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

DECEMBER 31, 2004
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INDEPENDENT AUDITOR'S REPORT

To the Board of County Road Commissioners
of Bay County
Kawkawlin, Michigan

We have audited the accompanying basic financial statements of the Bay County Road Commission, a component unit of Bay County, Michigan, as of December 31, 2004, and for the year then ended. These financial statements are the responsibility of the Road Commission management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Road Commission of Bay County, Michigan, as of December 31, 2004, and the results of its operations for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report, dated April 7, 2005, on our consideration of the Road Commission of Bay County, Michigan's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*, and should be considered in assessing the results of our audit.

The accompanying management's discussion and analysis on pages 3-7 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements of the Bay County Road Commission. The schedules on pages 26-28 are presented for purposes of additional analysis and are not a required part of the basic financial statements of the Road Commission of Bay County, Michigan. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

A handwritten signature in cursive script, reading "Stewart, Beaumont Whipple".

Certified Public Accountants

April 7, 2005

BAY COUNTY ROAD COMMISSION

A Component Unit of Bay County, Michigan

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the Bay County Road Commission (the "Road Commission"), we offer readers of these financial statements this narrative, overview and analysis of the financial activities of the Road Commission for the year ended December 31, 2004. This discussion and analysis is designed to assist the reader in focusing on the significant financial issues and activities and to identify any significant changes in financial position.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to provide a basis of understanding of the Bay County Road Commission's basic statements. These basic financial statements comprise three components: (1) government-wide financial statements, (2) fund financial statements and (3) notes to the financial statements. Supplementary financial information is also provided for additional information purposes.

Government-Wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the Road Commission finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on all of the Road Commission assets and liabilities, with the differences between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Road Commission is improving or deteriorating.

The *statement of activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

Fund Financial Statements

Unlike the government-wide financial statements, governmental financial statements focus on near-term inflows and outflows of spendable resources, as well as on the balances of spendable resources available at the end of the year. Such information may be useful in evaluating the Road Commission's near term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for the government-wide financial statements. By doing so, readers may better understand the long-term impact of the Road Commission's near-term financing decisions.

Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balance provide a reconciliation to facilitate this comparison between governmental funds and the government-wide financial statements.

The Bay County Road Commission adopts an annual appropriated budget for the operating fund. A budgetary comparison statement has been provided to demonstrate compliance with this budget.

Notes to the Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 11-25 of this report.

FINANCIAL HIGHLIGHTS

Government-Wide Financial Analysis

Statement of Net Assets

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. The net assets are separated into three major components, investment in capital assets, restricted net assets for primary and local roads and unrestricted net assets, which may be used to meet the ongoing obligations to citizens and creditors. The Road Commission's capital assets increased 6.3% from a year ago. The increase is primarily due additional road and bridge improvements added to the capital assets in 2004. Current and other restricted assets increased great than short-term liabilities decreased. The result was a decrease in restricted and unrestricted net assets of approximately \$1,980,000.

The table below shows a comparison of the net assets (in thousands of dollars) as of December 31, 2004 and 2003 in a condensed format.

	<u>2004</u>	<u>2003</u>
Assets		
Current and other unrestricted assets	\$ 5,386,384	\$ 6,791,679
Capital Assets	<u>76,122,954</u>	<u>70,414,277</u>
Total Assets	<u>81,509,338</u>	<u>77,205,956</u>
Liabilities		
Long-term liabilities outstanding	876,687	747,803
Other liabilities	<u>769,377</u>	<u>1,173,501</u>
Total Liabilities	<u>1,646,064</u>	<u>1,921,304</u>
Net Assets:		
Invested in capital assets	76,122,954	70,414,277
Restricted	944,679	2,291,696
Unrestricted	<u>2,795,641</u>	<u>2,578,679</u>
Total net assets	<u>\$79,863,274</u>	<u>\$75,284,652</u>

Statement of Activities

The following schedule compares the revenues and expenses (in thousands of dollars) for the current and previous fiscal years.

	<u>2004</u>	<u>2003</u>
Revenues		
Federal sources	\$ 1,317,634	\$ 1,595,103
State sources	8,741,499	8,264,030
Local sources	2,426,682	1,428,862
Charges for services	1,639,855	1,491,053
Other	<u>234,143</u>	<u>235,929</u>
Total Revenues	<u>14,359,813</u>	<u>13,014,977</u>
Expenses		
Maintenance	6,267,757	5,828,071
Administrative	1,104,002	708,039
Equipment (Net)	(1,220,628)	(897,652)
Depreciation	<u>3,630,060</u>	<u>3,440,953</u>
Total Expenses	<u>9,781,191</u>	<u>9,079,411</u>
Change in Net Assets	4,578,622	3,935,566
Prior Period Adjustment	-	-
Net Assets – Beginning of Year	<u>75,284,652</u>	<u>71,349,086</u>
Net Assets – End of Year	<u>\$79,863,274</u>	<u>\$ 75,284,652</u>

As shown in the preceding schedule comparing 2004 and 2003 Statement of Activities amounts, the total revenue increased \$1,344,836 or 10%. A large portion of the change between the years resulted from an increase of \$997,820 in local sources. The increase in local sources was due to the Road Commission reinstating the Build Better Local Road Program (BBCRP) in 1993, resulting in increased contributions from the Townships to supplement Road Commission match.

The balance of the revenue sources remained relatively constant between 2004 and 2003. Of the state source revenue, approximately \$8,300,000 and \$7,900,000 was received in 2004 and 2003, respectively from Michigan Transportation Funds which represents approximately 59% of the total revenue received in both years.

Total expenses increased from 2003 to 2004 by \$701,780 or 8%.

Government Funds Financial Analysis

As noted earlier, the focus of the fund (modified accrual) financial statements is to provide information on the near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Road Commission's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the year.

As of the end of the current year, the Road Commission reported an ending fund balance of \$4,101,120 a decrease of \$1,045,819 from the prior year. Approximately 74% or \$3,018,927 of the fund balance constitutes unreserved fund balance, which is available for spending at the government's discretion. The remainder of the fund balance is reserved to indicate that the amount is not available for new spending because \$137,514 has been prepaid and \$944,679 has been reserved for expenditures related to primary roads as required by the Michigan Department of Transportation.

BUDGETARY HIGHLIGHTS

The total difference between the original budget and the final amended budget was a difference in appropriations of approximately \$293,000 or approximately 2% of original budget expenditures. The decrease was predominately the result of decreasing local structure and bridge maintenance projects.

The variance between the final budget and the actual amounts was a negative amount of approximately \$842,211 or approximately 6% of the final budget expenditures. The negative variance for local construction was the result of not budgeting for private roads being turned over to the Road Commission. The private roads are also reported as other local contributions.

Detail of the original budget, final amended budget and actual amounts may be seen on page 10 of the basic financial statements.

CAPITAL ASSETS

Capital Assets – As of year end, the Road Commission had \$76,122,954 invested in capital assets (net of accumulated depreciation) as reflected in the following schedule, representing an increase of \$5,708,677 or approximately 8% from the 2003 balance. As stated earlier, the restatement was the result of reclassification of infrastructure assets from depreciable roads to non-depreciable land improvements.

	<u>2004</u>	<u>2003</u>
Land	\$ 472,961	\$ 460,072
Land improvements and right-of-ways	37,504,422	34,932,028
Buildings & Improvements	1,027,985	1,027,872
Equipment	2,888,505	2,936,920
Depletable assets	40,886	40,886
Infrastructure	<u>34,188,195</u>	<u>31,016,499</u>
Total Capital Assets	<u>\$ 76,122,954</u>	<u>\$ 70,414,277</u>

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Road Commission major revenue streams continue to be stable. Long-term state fiscal crises could, however, affect local township's demands for maintenance projects. It is anticipated that there will be an increase in Michigan Transportation Fund revenue in 2004 along with an increase in federal and state projects administered by the MDOT.

The Road Commission has budgeted for Primary Heavy Maintenance road and bridge projects to increase, however other expenditures are expected to remain relatively constant. It is anticipated that a transfer from primary to local roads will be required again in 2004 to offset an anticipated fund balance deficit in local roads. An overall reduction in fund balance of \$925,907 is anticipated.

CONTACTING THE ROAD COMMISSION MANAGEMENT

This financial report is designed to provide a general overview of the Bay County Road Commission's finances and to show accountability. Questions concerning any of the information provided in this report or request for additional financial information should be addressed to the Bay County Road Commission, 2600 E. Beaver Road, Kawkawlin, Michigan, 48631.

BASIC FINANCIAL STATEMENTS

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

GOVERNMENTAL FUND BALANCE SHEET/STATEMENT OF NET ASSETS
DECEMBER 31, 2004

	Governmental Fund	Adjustments (Note 2)	Statement of Net Assets
ASSETS			
Cash and cash equivalents	\$ 2,061,999	\$ -	\$ 2,061,999
Due from other governmental units -			
State	1,513,785	-	1,513,785
Local	754,629	-	754,629
Due from primary government	1,452	-	1,452
Due from other component units	32,133	-	32,133
Accounts receivable	5,675	-	5,675
Interest receivable	1,408	-	1,408
Prepaid expenditures/expenses	137,514	90,158	227,672
Inventory	787,631	-	787,631
Capital assets, net of accumulated depreciation			-
Assets being depreciated	-	38,145,571	38,145,571
Assets not being depreciated	-	37,977,383	37,977,383
Total Assets	<u>\$ 5,296,226</u>	<u>\$ 76,213,112</u>	<u>\$ 81,509,338</u>

LIABILITIES AND FUND EQUITY

Liabilities:

Accounts payable	\$ 119,417	\$ -	\$ 119,417
Accrued liabilities	60,386	-	60,386
Due to other governmental units	545	-	545
Deferred revenue	425,729	(425,729)	-
Advances and deposits	589,029	-	589,029
Noncurrent liabilities			
Due within one year		53,000	53,000
Due in more than one year	-	823,687	823,687
Total Liabilities	<u>1,195,106</u>	<u>450,958</u>	<u>1,646,064</u>

Fund Balance:

Fund Balance -			
Reserved -			
Prepaid expenditures	137,514	(137,514)	-
Primary roads	944,679	(944,679)	-
Unreserved -			
Undesignated	3,018,927	(3,018,927)	-
Total Fund Balance	<u>4,101,120</u>	<u>(4,101,120)</u>	<u>-</u>
Total Liabilities and Fund Balance	<u><u>\$ 5,296,226</u></u>		

Net Assets:

Invested in capital assets		76,122,954	76,122,954
Restricted -			
Primary roads		944,679	944,679
Unrestricted		2,795,641	2,795,641
Total Net Assets		<u><u>\$ 79,863,274</u></u>	<u><u>\$ 79,863,274</u></u>

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

**STATEMENT OF GOVERNMENTAL FUND REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE/STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2004**

	Governmental Fund	Adjustments (Note 2)	Statement of Activities
Revenues:			
Permits	\$ 33,331	\$ -	\$ 33,331
Intergovernmental -			
Federal sources	1,317,634	-	1,317,634
State sources	8,741,499	-	8,741,499
Local sources	2,386,261	40,421	2,426,682
Charges for services	1,639,855	-	1,639,855
Interest and rents	49,218	-	49,218
Other	151,594	-	151,594
Total Revenues	<u>14,319,392</u>	<u>40,421</u>	<u>14,359,813</u>
Expenditures/Expenses:			
Current -			
Local construction	902,583	(902,583)	-
Primary heavy maintenance	4,021,141	(4,021,141)	-
Local heavy maintenance	3,402,052	(3,402,052)	-
Primary maintenance	2,140,056	41,696	2,181,752
Local maintenance	2,502,477	48,947	2,551,424
State maintenance	1,553,013	(18,432)	1,534,581
Administrative	1,104,002	-	1,104,002
Equipment	2,544,998	(968,371)	1,576,627
Less equipment rental charged			
other activities	(2,797,255)	-	(2,797,255)
Depreciation	-	3,630,060	3,630,060
Capital Outlay	1,013,052	(1,013,052)	-
Less depreciation credit and retirements	(1,020,908)	1,020,908	-
Total Expenditures/Expenses	<u>15,365,211</u>	<u>(5,584,020)</u>	<u>9,781,191</u>
Excess of revenues over (under) expenditures/expenses	(1,045,819)	5,624,441	4,578,622
Fund Balance/Net Assets at January 1, 2004	<u>5,146,939</u>	<u>70,137,713</u>	<u>75,284,652</u>
Fund Balance/Net Assets at December 31, 2004	<u><u>\$ 4,101,120</u></u>	<u><u>\$ 75,762,154</u></u>	<u><u>\$ 79,863,274</u></u>

See Notes to Financial Statements

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

**STATEMENT OF GOVERNMENTAL FUND REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE
BUDGET AND ACTUAL
FOR THE YEAR ENDED DECEMBER 31, 2004**

	Original Budget	Final Budget	Actual	Variance with Amended Budget Positive (Negative)
Revenues:				
Permits	\$ 30,000	\$ 38,000	\$ 33,331	\$(4,669)
Intergovernmental -				
Federal sources	2,329,603	1,320,000	1,317,634	(2,366)
State sources	9,169,295	9,054,000	8,741,499	(312,501)
Local sources	981,250	2,240,000	2,386,261	146,261
Charges for services	1,144,609	1,332,000	1,639,855	307,855
Interest and rents	125,000	107,000	49,218	(57,782)
Other	110,000	109,000	151,594	42,594
Total revenues	<u>13,889,757</u>	<u>14,200,000</u>	<u>14,319,392</u>	<u>119,392</u>
Expenditures:				
Current -				
Local construction	-	735,000	902,583	(167,583)
Primary heavy maintenance	3,706,312	3,200,000	3,517,881	(317,881)
Local heavy maintenance	1,535,393	1,800,000	2,010,522	(210,522)
Primary structure and bridges	865,035	500,000	503,260	(3,260)
Local structure and bridges	2,338,915	1,350,000	1,391,530	(41,530)
Primary routine maintenance	1,292,500	1,500,000	915,028	584,972
Local routine maintenance	1,948,500	1,900,000	1,861,479	38,521
Primary traffic services	239,500	200,000	271,178	(71,178)
Local traffic services	194,000	100,000	140,779	(40,779)
Primary snow and ice control	503,000	600,000	953,850	(353,850)
Local snow and ice control	209,000	350,000	500,219	(150,219)
State trunkline maintenance	1,084,609	1,200,000	1,423,825	(223,825)
State trunkline non maintenance	50,000	125,000	129,188	(4,188)
Administrative- Primary	360,379	525,000	524,507	493
Administrative-local	339,621	363,000	579,495	(216,495)
Equipment - net	135,000	110,000	(252,257)	362,257
Capital Outlay - net	7,900	(35,000)	(7,856)	(27,144)
Debt service-Interest	6,000	-	-	-
Total Expenditures	<u>14,815,664</u>	<u>14,523,000</u>	<u>15,365,211</u>	<u>(842,211)</u>
Excess of revenues under expenditures	(925,907)	(323,000)	(1,045,819)	(722,819)
Fund Balance at January 1, 2004	<u>4,811,141</u>	<u>5,146,939</u>	<u>5,146,939</u>	<u>-</u>
Fund Balance at December 31, 2004	<u>\$ 3,885,234</u>	<u>\$ 4,823,939</u>	<u>\$ 4,101,120</u>	<u>\$(722,819)</u>

See Notes to Financial Statements

NOTES TO FINANCIAL STATEMENTS

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The financial statements of the Bay County Road Commission, a component unit of the County of Bay, Michigan, have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to governmental entities. The more significant accounting policies are described as follows:

A. Description of Road Commission Operations –

The Bay County Road Fund, referred to as the Road Commission, is a Component Unit of the County of Bay, Michigan, and is used to control the expenditure of revenues from the State distribution of gas and weight taxes, federal awards, reimbursements from the Department of State Highways for work performed by the County on State trunklines and contributions from other local units of government (townships) for work performed by the Road Commission work force. The Road Fund is the only fund of the Road Commission.

The Road Commission, which is established pursuant to the County Road Law (MCL224.1), operates under an elected Board of three (3) County Road Commissioners who establish policies and review operations of the Road Commission. The Road Commission provides services to fourteen (14) Townships in Bay County and maintains over 1,200 miles of state, local and primary roads.

B. Measurement Focus, Basis of Accounting and Financial Statement Presentation –

The government-wide financial statement columns (i.e., statement of net assets and statement of activities) are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grant and similar items are recognized as revenues as soon as all eligibility requirements imposed by the provider have been met.

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized when it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the year. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, expenditures relating to compensated absences, and claims and judgments are recorded only when payment is due.

C. Assets, Liabilities, and Fund Balance or Net Assets –

Cash and Cash Equivalents - Cash equivalents are short-term investments that are readily convertible to cash or have a maturity date of 90 days or less from the date of purchase. Cash equivalents include certificates of deposit, commercial paper and investment trust funds and are recorded at cost which approximates fair value. The pooled investment funds have the general characteristics of demand deposit accounts in that the Road Commission may deposit additional cash at any time and effectively may withdraw cash at any time without prior notice or penalty.

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (cont'd):

Inventories – Inventories of road materials and equipment parts are recognized using the consumption method (inventories are recorded as expenditures when they are used). Inventories are stated at the lower of average cost or market.

Prepaid Items – Certain payments to vendors (particularly for insurance coverage) reflect costs that are applicable to a future period and are recorded as prepaid items.

Capital Assets – Capital assets, which include property, plant, equipment, and infrastructure are reported in the government-wide (statement of net assets) financial statements. Capital assets for land, buildings and improvements and all equipment except road equipment are defined by the Road Commission as assets with an initial, individual cost of \$2,000 or more and an estimated useful life in excess of 2 years. Road equipment is capitalized as defined by the Michigan Department of Transportation without consideration of a minimum cost. Capital assets are recorded at historical cost or estimated if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Capital assets are recorded in the governmental fund statements as capital expenditures at the time of purchase.

Depreciation is computed on the sum-of-the-years digits method for road equipment, and straight-line method for all other capital assets over the estimated useful life of the related asset.

The estimated useful lives are as follows:

Buildings and Improvements	40 years
Equipment	5- 8 years
Roads	8-30 years
Bridges	25-50 years
Traffic signals	15 years

Infrastructure is reported retrospectively from 1980, except for right-of-ways, bridges, and traffic signals which are required to be reported despite the date of purchase. Roads are removed from the capital assets at the time the group of individually recorded roads have been fully depreciated.

Depletion is calculated as the amount of prorated cost or other indicated value assigned to the extracted portion of a natural resource (gravel).

The Uniform Accounting Procedures Manual for Michigan County Road Commissions provides for recording depreciation and depletion in the governmental fund statements as a charge to various expenditures accounts, and a credit to a depreciation/depletion credit account. Accordingly, the annual depreciation/depletion expenditures do not affect the available operating equity of the governmental fund statements.

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (cont'd):

Accrued Vacation and Sick Pay – In accordance with contracts negotiated with the various employee groups, individual employees have vested right upon termination of employment to receive payments for unused vacation and sick leave under formulas and conditions specified in the contract. All amounts vested are accrued in the government-wide statements (statement of net assets).

Deferred Revenues – In both the government-wide and the fund financial statements revenue received or recorded before earned is recorded as deferred revenue. In addition, in the governmental fund statements revenues that are not both measurable and available are recorded as deferred revenues.

Advances From The State of Michigan – The State of Michigan advances funds on a State maintenance agreement it has with the Bay County Road Commission for specified maintenance which the Road Commission will perform during the year and for equipment purchased and used in performance of the specified maintenance. These advances are considered current liabilities because they are subject to repayment annually upon audit by the State of Michigan.

Equipment Rentals – The Michigan Department of Transportation requires that the cost of operating equipment, including depreciation, be allocated to the various activities. The effect of this allocation is offset to equipment expenditures/expenses.

Fund Equity – Designation of fund balance represents tentative management plans that are subject to change.

Estimates – In preparing financial statements in conformity with U.S. generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTE 2 - RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS:

- A.** Explanation of differences between the governmental fund balance sheet and the government-wide statement of net assets (Page 8).

Fund Balance – governmental fund	\$ 4,101,120
Capital assets used in the governmental fund statements that are not financial resources and therefore not reported in the governmental fund financial statements	
Add – capital assets	110,445,345
Deduct – accumulated depreciation	(34,322,391)

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003

NOTE 2 - RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS - (cont'd):

Long-term liabilities that are not due in the current period therefore not reported in the governmental fund statements	\$ (876,687)
Prepaid expenses not reported in the governmental fund statements	90,158
Revenues that have been deferred in the governmental fund statements because they are not "available"	<u>425,729</u>
Net Assets	<u>\$ 79,863,274</u>

- B.** Explanation of differences between the governmental fund statement of revenues, expenditures and changes in fund balance and the government-wide statement of activities (Page 9).

Excess of revenues under expenditures – governmental fund statement	\$ (1,045,819)
The governmental fund statements report capital outlay as expenditures, however, in the government-wide Statement of Activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense	
Add – capital outlay and infrastructure	9,338,828
Deduct – retirements	(91)
Deduct – depreciation	(3,630,060)
Revenues deferred in the governmental fund statements because they do not provide current financial resources that are reported in the government-wide Statement of Activities	40,421
Prepaid expense adjustment not reported in the governmental fund statements	4,227
Accrued vacation and sick time and worker's compensation expenses not reported in the governmental fund statements because they will not be paid with current financial resources	<u>(128,884)</u>
Change in Net Assets	<u>\$ 4,578,622</u>

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 3 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY:

Auditing and Reporting –

The audit was performed in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in ***Government Auditing Standards***, issued by the Comptroller General of the United States as described in the Independent Auditor's Report, but also with the standards as provided in Act No. 71 of Public Acts of 1919, Section 21.41 of the Michigan Compiled Laws.

The financial statements were prepared in accordance with accounting principles generally accepted in the United States of America as described in the Independent Auditor's Report, but also with applicable rules of the Michigan State Department of Transportation.

Budgetary Compliance –

The Engineer-Manager of the Road Commission prepares from data submitted by the administrative staff a proposed operating budget for the calendar year commencing January 1. The operating budget includes proposed expenditures and resources to finance them. The budget is approved at the activity level by the Board of County Road Commissioners.

The budget for the General Operating Fund is adopted on the modified accrual basis which is consistent with accounting principles generally accepted in the United States of America.

Prior to December 31, the proposed budget is presented to the Board of County Road Commissioners. The Board holds a public hearing and may add to, subtract from, or change appropriations. The budget is then legally enacted through passage of a Board of County Road Commissioner's Resolution. After the budget is adopted, the Engineer-Manager is authorized to transfer amounts between items of the adopted budget at year end to reflect the effects of the distribution of the distributive account. All amendments to the budget must have direct approval of the Board of County Road Commissioners.

The Road Commission does not employ encumbrance accounting as an extension of formal budgetary integration. All annual appropriations lapse at year end.

Michigan Public Act 621 of 1978, Section 18(1), as amended, provides that a governmental unit shall not incur expenditures in excess of the amount appropriated at the legally adopted level. During the year ended December 31, 2003, the Road Commission had twelve over-expenditures as reported on the Statement of Governmental Fund Revenues, Expenditures and Changes in Fund Balance – Budget and Actual.

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 4 - DEPOSITS AND INVESTMENTS:

The Uniform Accounting Procedures Manual for Michigan County Road Commissions provides that the County Treasurer maintain the cash of the Road Commission. All Road Commission receipts are deposited with the Bay County Treasurer's Office, and in order to make disbursements, the Bay County Road Commission requests the County Treasurer to transfer the required funds to an imprest vendor or payroll checking account. Also, in order to invest cash, a request is made to the County Treasurer.

Bay County is authorized through its investment policy, which is in accordance with Act 20 PA 1943 as amended by Act 196 PA 1997, to invest the Road Commission surplus funds in the following types of investments:

- a) In bonds, securities and other direct obligations of the United States or an agency or instrumentality of the United States.
- b) In certificates of deposit, savings accounts, deposit accounts or depository receipts of a financial institution, but only if the bank, savings and loan association, or credit union is eligible to be a depository of surplus funds belonging to the State under Section 5 or 6 of Act No. 105 of the Public Acts of 1855, as amended, being section 21.145 and 21.146 of the Michigan Compiled Laws.
- c) In commercial paper rated at the time of purchase within the two (2) highest classifications established by not less than two (2) standard rating services and which matures not more than 270 days after the date of purchase.
- d) In the United States government or federal agency obligations repurchase agreements.
- e) In bankers acceptances of United States banks.
- f) In obligations of the State of Michigan or any of the political subdivisions that at the time of purchase are rated as investment grade by not less than one standard rating service.
- g) In mutual funds registered under the investment company Act of 1940, with the authority to purchase only investment vehicles that are legal for direct investment by a public corporation.
- h) In investment pools organized under the surplus funds investment act, 367 of 1982.
- i) In investment pools organized under the local government investment pool act, 121 of 1985.

Deposits -

As a component unit of Bay County, all Road Commission cash and cash equivalents are a part of the accounts maintained by Bay County at banking institutions insured by federal depository insurance. However, the Road Commission by State statute has funds allocated to it by the State of Michigan for its exclusive use and control. As a result, funds of the Road Commission have separate insurance coverage.

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 4 - DEPOSITS AND INVESTMENTS - (cont'd):

Federal Deposit Insurance Corporation (FDIC) regulations provide that deposits of governmental units are to be separately insured for the amount of \$100,000 for deposits in an insured bank for savings deposits and \$100,000 for demand deposits. Furthermore, if specific deposits are regulated by statute or bond indenture, these specific deposits are to be separately insured for the amount of \$100,000.

As of December 31, 2004, the carrying amount of the Road Commission's deposits is \$865,437, and the bank balance is \$1,073,375. The bank balance is classified by credit risk as follows:

Bank accounts - insured by FDIC	\$ 111,504
Bank accounts – uninsured and uncollateralized	161,871
Certificate of deposit - insured by FDIC	100,000
Certificate of deposit - uninsured and uncollateralized	<u>700,000</u>
	<u>\$ 1,073,375</u>

The County believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the County evaluates each financial institution and assesses the level of risk. The County uses only those financial institution with an acceptable estimated risk level as depositories.

Investments -

As of December 31, 2004, the Road Commission investments are susceptible to the following risk categories as summarized in the table below:

- 1) Insured or registered for which the securities are held by the Road Commission or its agent in the Road Commission.
- 2) Uninsured and unregistered for which the securities are held by the trust department or a bank in the Road Commission's name.
- 3) Uninsured and unregistered for which the securities are held by the trust department of a bank but not in the Road Commission's name.

	<u>Categories</u>			<u>Carrying</u>
	<u>1</u>	<u>2</u>	<u>3</u>	<u>Amount</u>
Commercial Paper	<u>\$ -</u>	<u>\$ 899,362</u>	<u>\$ -</u>	\$ 899,362
Government Investment – Trust Funds				<u>297,000</u>
				<u>\$ 1,196,362</u>

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 4 - DEPOSITS AND INVESTMENTS - (cont'd):

The Government Investment Trust Funds are funds deposited in National City Bank Funds Investment, which are managed by the bank's trust department. The trusts invest primarily in short-term maturity U.S. Government backed or guaranteed securities which are held by the trust in its name. These funds have not been considered to be susceptible to investment risk categories. The investment pool accounts are registered with the Securities and Exchange Commission and the fair value of the County's portion in the investment pools is the same as the value of the investment pool shares. The investment pools have been reported in the financial statements as a cash equivalent because they have the general characteristics of demand deposit accounts in that the County may deposit additional cash at any time and effectively may withdraw cash at any time without prior notice or penalty. The investment pools are recorded at cost which approximates fair value.

Also the caption cash and cash equivalents on the Balance Sheet also includes commercial paper with a maturity date less than 90 days and \$200 in petty cash.

NOTE 5 - DUE FROM OTHER GOVERNMENTAL UNITS:

Due from other government units as of December 31, 2004 consists of the following:

State –	
Motor Vehicle Highway Funds	\$ 1,275,389
Trunkline Maintenance	230,693
Transportation Department – Other	<u>7,703</u>
	<u>1,513,785</u>
Local –	
Township road agreements	749,765
Other	<u>4,864</u>
	<u>754,629</u>
	<u>\$ 2,268,414</u>

The governmental fund statements report deferred revenue in connection with receivables that are not considered to be available to liquidate liabilities of the current period. Both the government-wide and the governmental fund statements defer revenue recognition in connection with resources that have been received, but not earned. At the end of the current year deferred revenue in the governmental fund consisted of Township road agreement receivables in the amount of \$425,729 that are considered to be unavailable at December 31, 2004.

NOTE 6 - INVENTORIES:

The inventory balance of \$787,631 at December 31, 2004 consisted of \$379,156 of road materials and \$408,475 of equipment parts and materials.

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 7 - CAPITAL ASSETS:

Capital assets activity for the current year was as follows:

	Balance December 31, <u>2003</u>	<u>Additions</u>	<u>Deletions</u>	<u>Removals</u>	Balance December 31, <u>2004</u>
Capital Assets, not being depreciated –					
Land	\$ 460,072	\$ 12,889	\$ -	\$ -	\$ 472,961
Land Improvements	34,582,367	2,572,394	-	-	37,154,761
Right of Ways	<u>349,661</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>349,661</u>
Total Capital Assets, not being depreciated	<u>35,392,100</u>	<u>2,585,283</u>	<u>-</u>	<u>-</u>	<u>37,977,383</u>
Capital Assets, being depreciated –					
Buildings and Improvements	2,340,844	61,822	-	-	2,402,666
Road Equipment	8,773,529	914,264	464,877	-	9,222,916
Shop Equipment	120,893	8,477	-	-	129,370
Office Equipment	155,320	14,264	-	-	169,584
Engineering Equipment	102,728	1,336	-	-	104,064
Yard and Storage	1,294,302	-	-	-	1,294,302
Infrastructure -					
Roads	40,047,933	3,858,592	-	1,845,275	42,061,250
Bridges	14,991,900	1,894,790	-	150,000	16,736,690
Traffic Signals	294,083	-	-	-	294,083
Depletable assets –					
Gravel Pits	<u>53,037</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>53,037</u>
	<u>68,174,569</u>	<u>6,753,545</u>	<u>464,877</u>	<u>1,995,275</u>	<u>72,467,962</u>
Less – accumulated depreciation for –					
Buildings and Improvements	1,312,972	61,709	-	-	1,374,681
Road Equipment	6,707,594	906,356	464,786	-	7,149,164
Shop Equipment	85,656	8,353	-	-	94,009
Office Equipment	88,707	13,828	-	-	102,535
Engineering Equipment	63,047	4,639	-	-	67,686
Yard and Storage	564,848	53,489	-	-	618,337
Infrastructure –					
Roads	17,870,033	2,246,405	-	1,845,275	18,271,163
Bridges	6,231,287	322,344	-	150,000	6,403,631
Traffic Signals	216,097	12,937	-	-	229,034
Depletable Assets	<u>12,151</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>12,151</u>
	<u>33,152,392</u>	<u>3,630,060</u>	<u>464,786</u>	<u>1,995,275</u>	<u>34,322,391</u>
Total Capital Assets, being depreciated, net	<u>35,022,177</u>	<u>3,123,485</u>	<u>91</u>	<u>-</u>	<u>38,145,571</u>
Governmental activity capital assets, net	<u>\$ 70,414,277</u>	<u>\$ 5,708,768</u>	<u>\$ 91</u>	<u>\$ -</u>	<u>\$ 76,122,954</u>

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 7 - CAPITAL ASSETS - (cont'd):

The State of Michigan does not allow depreciation to be recorded in the governmental fund statements on salt barn construction costs reimbursed by the State. However, the depreciation of \$27,776 on the salt barn is recorded in the government-wide statement of activities. Total depreciation for the year ended December 31, 2004 was \$3,630,060.

NOTE 8 - FEDERAL AWARDS:

It is required by the Michigan Department of Transportation (MDOT) that Road Commissions report total federal awards for Highway Research, Planning and Construction pertaining to their County. However, only the federal awards applicable to force account expenditures are required to be audited for compliance under the Single Audit Act through Road Commission procurement. The reason for this requirement is that the Road Commission is required to have accounting and administrative control over the force account portion while the balance is administered by MDOT.

During the year ended December 31, 2004, the Road Commission of Bay County had less than \$300,000 of force account expenditures applicable to federal awards (local force revenue). As a result, an audit for compliance under the Single Audit Act has not been performed.

The federal revenues of \$1,317,634 represent the Department of Transportation Federal Highway grant money expended on public road improvement projects which were administered by the Michigan Department of Transportation, however are required to be reported by the Road Commission.

NOTE 9 - ADVANCES AND DEPOSITS:

Advances and deposits of \$589,029 at December 31, 2004, represent money advanced by the State of Michigan under the maintenance contract the Road Commission has with the State, money advanced by the State for equipment purchases, and deposits from contractors and individuals for various projects. Both State advances are adjusted annually by the State and must be repaid if the maintenance contract is canceled. The following is a summary of the balance by source and use:

State -	
Trunkline maintenance	\$ 87,926
Equipment	<u>396,808</u>
	484,734
Local -	
Contractors and Individuals -	
Performance deposits	<u>104,295</u>
	<u>\$ 589,029</u>

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 10 - LONG-TERM LIABILITIES:

The following is a summary of the changes in long-term liabilities of the Road Commission for the year ended December 31, 2004:

	Balance January 1, 2004	Additions	Reductions	Balance December 31, 2004	Due Within One Year
Accrued sick and vacation	\$ 747,803	\$ -	\$ 46,116	\$ 701,687	\$ -
Accrued claims liability	<u>-</u>	<u>221,900</u>	<u>46,900</u>	<u>175,000</u>	<u>53,000</u>
	<u>\$ 747,803</u>	<u>\$ 221,900</u>	<u>\$ 93,016</u>	<u>\$ 876,687</u>	<u>\$ 53,000</u>

Accrued Sick and Vacation

Employees are granted vacation and sick leave in varying amounts based on the Commission's administrative policy and contract with union employees. Vacation time is credited annually to each employee, but cannot be accumulated for more than one year without Board approval, with the exception that all employees can carry over five days without Board approval. Administrative employees and union employees are limited to 1,200 hours sick leave accumulation. At this point, the employees are allowed to accumulate 96 hours of sick leave reserve, of which the unused portion is paid by the Road Commission at the beginning of the following year. Upon retirement, permanent disability or leaving the employment of the Road Commission, all union employees are paid 85 percent of their accumulated sick leave. Administrative employees are paid 85 percent of their accumulated sick leave upon leaving the employment of the Road Commission. The dollar amount of these vested rights which has been accrued on the financial statements amounted to approximately \$522,213 for sick leave and \$179,474 for vacation at December 31, 2004.

Accrued Claims Liability -

The County has estimated accrued outstanding workers' compensation insurance claims including an estimate for the claims incurred but not reported (IBNR). The dollar amount of these claims, which has been accrued on the financial statements, is estimated to amount to approximately \$175,000 at December 31, 2004.

NOTE 11 - EMPLOYEE PENSION:

Plan Description -

The Bay County Road Commission, as a component unit of Bay County, participates in the Bay County Retirement System. The Retirement system is a single employer, defined benefit pension plan, which was established by County ordinance to provide retirement and pension benefits for substantially all employees of Bay County. The benefit provisions are governed by Michigan Public Act of 1984, as amended.

The County issues a publicly available Annual Financial Report that includes financial statements for the plan. That report may be obtained from Bay County by writing to the Bay County Employees Retirement System, Bay County Building, 515 Center Avenue – Suite 706, Bay City, MI 48708-6128.

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 11 - EMPLOYEE PENSION - (cont'd):

Funding Policy -

The County's policy is to fund normal costs which are based on actuarially determined rates, expressed as percentages of annual covered payroll, and which are sufficient to accumulate assets to pay benefits when due. The provisions of the Plan requires the County to contribute at an actuarially determined rate. The current rate for the County and Road Commission employees is 0% of annual covered payroll. Plan members contribute at a rate of 4% of their annual covered salary. The County pays the plan member contributions for all employee groups. The Plan benefit provisions and contribution requirements of plan members and the County are established and may be amended by the Board of Commissioners in accordance with County policies, union contracts, and plan provisions.

Annual Pension Costs

During the year ended December 31, 2004, the County's annual pension cost of \$0 was equal to the County's required and actual contributions. The Road commission paid plan member contribution of \$144,081 for the year ended December 31, 2004.

The required contribution rate was determined as part of the December 31, 2003 actuarial valuation using the individual entry age normal cost method. The actuarial assumption included (a) 7.5% net investment rate of return, and (b) project salary increases of 5% to 12% per year, which includes pay inflation at 4%. There are no projected cost of living adjustments. The actuarial value was determined using techniques that smooth the effect of short-term volatility in the market value of investment over a five year period. The Bay County unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll on an open basis. The amortization periods are 30 years for groups that are underfunded and 10 years for groups that are over funded. There is no unfunded accrued liability for the Road Commission.

Three-Year Trend Information

Fiscal Year Ending	Road Annual Pension Costs (APC)	Percentage of APC Contribution	Net Pension Obligation
December 31, 2002	\$ -	100 %	\$ -
December 31, 2003	-	100	-
December 31, 2004	-	100	-

NOTE 12 - POSTEMPLOYMENT:

In addition to the pension benefits described in Note 11, the Bay County Road Commission provides postemployment health care to eligible employees who retire from the Road Commission on or after attaining retirement age with at least ten years of service or age 60 with 8 years of service.

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 12 - POSTEMPLOYMENT - (cont'd):

During 2002, the Road Commission started participation in the Bay County Public Employee Health Care Fund where contributions are made annually to accumulate an amount to fund postemployment benefits (health care). The Road Commission contributed \$144,081 to the fund for the year end December 31, 2004. Along with this contribution, the Road Commission recognizes expenditures paid for postemployment health care benefits on a pay-as-you-go basis. For the year ended December 31, 2004 these health care costs amounted to approximately \$734,224 with 76 eligible participants.

NOTE 13 - SUMMARY OF DISCLOSURE OF SIGNIFICANT CONTINGENCIES:

In the normal course of its operations, the Bay County Road Commission often becomes a party to various claims and lawsuits. In the opinion of the Road Commission's legal counsel, if any of these claims should result in an unfavorable resolution to the Road Commission, the Road Commission's liability would be limited to its deductible under insurance policies. The insurer would pay the losses, and there should be no material effect on the financial position of the Road Commission.

Also, as part of its trunkline maintenance agreement with the State of Michigan, the Road Commission's costs charged to the State are subject to audit. The amounts, if any, which may have to be paid back to the State, cannot be determined at this time, although the Road Commission expects such amounts, if any, to be immaterial.

NOTE 14 - RISK MANAGEMENT:

The Road Commission is a member of the Michigan County Road Commission Self-Insurance Pool established pursuant to the laws of the State of Michigan which authorizes contracts between municipal corporations (interlocal agreements) to form group self-insurance pools, and to prescribe conditions to the performance of these contracts.

The Michigan County Road Commission Self-Insurance Pool was established for the purpose of making a self-insurance pooling program available for Michigan County Road Commissions, which includes, but is not limited to, general liability coverages, auto liability coverages, property insurance coverages, stop loss insurance protection, claims administration, and risk management and loss control services pursuant to Michigan Public Act 138 of 1982.

The Bay County Road Commission pays an annual premium to the Pool for property (buildings and grounds) coverage, automobile liability, errors or omissions liability and bodily injury, property damage and personal injury liability. The agreement for the formation of the Pool provides that the Pool will be self-sustaining through member premiums and will purchase both specific and aggregate stop-loss insurance to the limits determined necessary by the Pool Board.

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 14 - RISK MANAGEMENT - (cont'd):

The Road Commission is self-insured for workers' compensation claims. Liabilities for workers' compensation claims are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities included a provision for claims that have been incurred but not reported (IBNRs). Claims liabilities are estimated based on actual claims filed subsequent to year-end.

The Road Commission continues to carry commercial insurance for employee health and accident insurance. The amount of settlements (claims) for the past three years have not exceeded insurance coverage.

NOTE 15 - EQUIPMENT EXPENDITURE NET BALANCE:

The Road Commission, in compliance with the Uniform Accounting Procedures Manual for Michigan County Road Commissions charges rental on Road Commission equipment used for various construction and maintenance projects performed by the Road Commission. The cost for this rental, which is based on a rental rate per hour established by the Michigan Department of Transportation multiplied by rental hours, is reported as an expenditure in the various maintenance activities. An expenditure credit is reported as an offset against the equipment expenditure activities. Accordingly, the equipment rental does not affect total expenditures or the available operating equity of the Road Commission's General Operating Fund. The net balance for the year ended December 31, 2004 is as follows:

	<u>Governmental Fund</u>	<u>Statement of Activities</u>
Equipment –		
Direct	\$ 1,474,738	\$ 568,381
Indirect	809,529	747,515
Operating	<u>260,731</u>	<u>260,731</u>
	2,544,998	1,576,627
 Less-equipment rental	 <u>(2,797,255)</u>	 <u>2,797,255</u>
	 <u>\$ (252,257)</u>	 <u>\$ (1,220,628)</u>

BAY COUNTY ROAD COMMISSION
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004

NOTE 16 - CAPITAL OUTLAY EXPENDITURES NET BALANCE:

On the governmental fund financial statements, the Road Commission reports a depreciation credit as an offset to capital outlay as a result of charging depreciation to various expenditure accounts as explained in Note 1. Retirements are also reported as a credit against capital outlay. The balance of \$7,856 is the result of the amount of depreciation and retirements being subtracted from capital outlay expenditures for the year ended December 31, 2004 as follows:

Capital Outlay –	
Land improvements, building	
and equipment	\$ 1,013,052
Less - depreciation/depletion	(1,020,817)
- retirements	(91)
	<u>\$ (7,856)</u>

SUPPLEMENTARY INFORMATION

BAY COUNTY ROAD COMMISSION
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DETAIL SCHEDULE OF REVENUES
GENERAL OPERATING FUND
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004	2003
Revenues:		
Permits	\$ 33,331	\$ 24,937
Federal Sources -		
Critical Bridge	1,317,634	-
Surface transportation program (STP)	-	1,595,103
	<u>1,317,634</u>	<u>1,595,103</u>
State Sources -		
Motor Vehicle Highway Funds - Act 51 -		
Engineering	10,000	10,000
Urban road	1,361,271	1,331,734
Allocation	6,976,257	6,554,278
Critical Bridge	-	-
STP program	-	-
Economic Development Fund - rural primary	393,971	368,018
	<u>8,741,499</u>	<u>8,264,030</u>
Local Sources -		
Township contributions	1,431,181	1,378,467
Other contributions	835,000	373,572
County appropriation	120,080	-
	<u>2,386,261</u>	<u>1,752,039</u>
Charges for Services -		
State Trunkline maintenance	1,484,660	1,340,441
State Trunkline nonmaintenance	129,188	149,046
Salvage sales	7,516	1,566
Other Inspection fees	18,491	-
	<u>1,639,855</u>	<u>1,491,053</u>
Interest and rent	<u>49,218</u>	<u>55,233</u>
Other -		
Sundry refunds	4,795	-
Gain on equipment disposal	84,860	106,843
Other	61,939	48,916
	<u>151,594</u>	<u>155,759</u>
Total Revenues	<u><u>\$ 14,319,392</u></u>	<u><u>\$ 13,338,154</u></u>

BAY COUNTY ROAD COMMISSION
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DETAIL SCHEDULE OF EXPENDITURES
GENERAL OPERATING FUND
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

	<u>2004</u>	<u>2003</u>
Expenditures:		
Construction -		
Local roads and structures	\$ 902,583	\$ 351,257
Heavy Maintenance -		
Primary roads and structures	4,021,141	4,489,297
Local roads and structures	<u>3,402,052</u>	<u>1,675,897</u>
	<u>7,423,193</u>	<u>6,165,194</u>
Maintenance -		
Primary roads and structures,		
winter and traffic control	2,140,056	1,939,365
Local roads and structures,		
winter and traffic control	<u>2,502,477</u>	<u>2,432,164</u>
	<u>4,642,533</u>	<u>4,371,529</u>
State Maintenance -		
State Trunkline maintenance	1,423,825	1,340,441
State Trunkline nonmaintenance	<u>129,188</u>	<u>149,046</u>
	<u>1,553,013</u>	<u>1,489,487</u>
Equipment -		
Direct	1,474,738	1,339,719
Indirect	809,529	792,528
Operating	260,731	178,290
Less - equipment rental	<u>(2,797,255)</u>	<u>(2,295,728)</u>
	<u>(252,257)</u>	<u>14,809</u>
Administrative -		
Administration	1,288,460	893,916
Less - overhead	(155,751)	(147,307)
- handling charges	(22,505)	-
- purchase discounts	<u>(6,202)</u>	<u>(5,758)</u>
	<u>1,104,002</u>	<u>740,851</u>
Capital Outlay -		
Land improvements, building		
and equipment	1,013,052	1,039,673
Less - depreciation/depletion	(1,020,817)	(974,241)
- retirements	<u>(91)</u>	<u>(4,903)</u>
	<u>(7,856)</u>	<u>60,529</u>
Total Expenditures	<u><u>\$ 15,365,211</u></u>	<u><u>\$ 13,193,656</u></u>

BAY COUNTY ROAD COMMISSION
A Component Unit of Bay County, Michigan

SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
BY FUND BALANCE SUB-ACCOUNTS
GENERAL OPERATING FUND
FOR THE YEAR ENDED DECEMBER 31, 2004

	<u>Primary</u>	<u>Local</u>	<u>County</u>	<u>Total</u>
Revenues:				
Permits	\$ 11,579	\$ 11,993	\$ 9,759	\$ 33,331
Intergovernmental -				
Federal Sources	309,763	1,007,871	-	1,317,634
State Sources	6,506,837	2,234,662	-	8,741,499
Local Sources	-	2,386,261	-	2,386,261
Charges for services	-	18,490	1,621,365	1,639,855
Interest and rents	-	10	49,208	49,218
Other	-	61,727	89,867	151,594
Total Revenues	<u>6,828,179</u>	<u>5,721,014</u>	<u>1,770,199</u>	<u>14,319,392</u>
Expenditures:				
Construction	-	902,583	-	902,583
Heavy maintenance	4,021,141	3,402,052	-	7,423,193
Maintenance	2,140,056	2,502,477	-	4,642,533
Other -				
Trunkline maintenance	-	-	1,423,825	1,423,825
Trunkline nonmaintenance	-	-	129,188	129,188
Administrative - net	524,507	579,495	-	1,104,002
Equipment - net	(81,328)	(94,773)	(76,156)	(252,257)
Capital outlay - net	-	-	(7,856)	(7,856)
Total Expenditures	<u>6,604,376</u>	<u>7,291,834</u>	<u>1,469,001</u>	<u>15,365,211</u>
Excess of revenues over (under) expenditures	223,803	(1,570,820)	301,198	(1,045,819)
Optional transfers	(1,570,820)	1,570,820	-	-
Fund balance at beginning of year	<u>2,291,696</u>	<u>-</u>	<u>2,855,243</u>	<u>5,146,939</u>
Fund balance at end of year	<u><u>\$ 944,679</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 3,156,441</u></u>	<u><u>\$ 4,101,120</u></u>

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING
STANDARDS***

To the Board of County Road
Commissioners of Bay County
Kawkawlin, Michigan

We have audited the financial statements of Bay County Road Commission, a component unit of Bay County, Michigan, as of and for the year ended December 31, 2004, and have issued our report thereon, dated April 7, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered Bay County Road Commission's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Bay County Road Commission's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management and Board of County Road Commissioners of the Bay County Road Commission and is not intended to be and should not be used by anyone other than these specified parties.


Certified Public Accountants

April 7, 2005

MANAGEMENT LETTER

Board of County Road Commissioners
Bay County Road Commission
Kawkawlin, Michigan

Members of the Board:

In planning and performing our audit of the financial statements of the Bay County Road Commission for the year ended December 31, 2004, we considered its internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting.

This is the second year that the Bay County Road Commission has been audited under the new Statement of Auditing Standards No. 99 "Consideration of Fraud in the Financial Statement Audit", which became effective for audits ending on or after December 31, 2003. SAS 99 put renewed emphasis on internal control over fraud and abuse in the workplace. It requires that we "brainstorm" on how fraud and abuse can be committed in an entity and design tests with this in mind. The new standard also requires improved communications with the client on possible areas of fraud and abuse. As a result, we believe that certain changes in your accounting and administrative procedures would enhance controls that the Road Commission has in place.

Reporting of Compensated Absences

The notes to financial statements in the Road Commissions annual financial statements are now required to disclose the increase and decrease in compensated absences, not just the net change. Also, the notes should disclose the amount of compensated absences due within one year of the date of the statement of net assets, even if an estimate must be made.

If the current accounting records for compensated absences do not make the above-described information available, we recommend that procedures be adopted that will capture the required amounts.

Control over Transfer Vouchers

At the present time, transfer vouchers (journal entries) include a description for the entry and are numbered and maintained in a binder for control purposes. However, not all transfer vouchers are required to be approved by a second individual.

Not having a procedure requiring that all transfer vouchers be approved allows for the possibility of inaccurate or fraudulent financial reporting.

We recommend that all transfer vouchers be approved by an individual that is able to analyze the accompanying information supporting the entry.

Reviewing accounting software applications

Cogitate has one of the few software packages that pertain specifically to Road Commissions. Thus, the software is designed to assist Road Commission accounting personnel in recording the substantial amount of detailed transactions that are required under the Michigan Department of Treasury accounting manual.

Through discussions with management and observations during the audit, we noted that a few accounting and reporting processes are not as efficient as we believe they possibly could be, particularly with the summarization of revenue and expenditure accounts.

We recommend that with the installation of the windows versions of the Cogitate software, that you consider changing the summarization of certain revenue and expenditure accounts.

Conforming to the Uniform Budgeting Act

As noted in the audited financial statements, several expenditures of the Road Commission exceeded the amounts appropriated.

Michigan Public Act 621 of 1978 Sec. 18 as amended, provides that a Road Commission shall adopt a formal budget and shall not incur expenditures in excess of the amounts appropriated. The Road Commission has established procedures to detect such violations, however we recommend that the budget be monitored more closely to assist in eliminating expenditures in excess of budget.

These conditions were considered in determining the nature, timing and extent of the audit tests applied in our audit of the December 31, 2004 financial statements. We have not considered internal control since the date of our report. It is important to remember that management is responsible for the design and implementation of programs and controls to prevent and detect fraud.

This report is intended solely for the information of management and the Board of Road Commissioners of the Bay County Road Commission and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

A handwritten signature in cursive script, appearing to read "Stewart, Beausaint Whipple".

April 7, 2005